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Nguyen, Joyce Freeman, and Christopher Hake

**UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF CALIFORNIA
SAN JOSE DIVISION**

In re) Case No. C 08-00201 JW
2)
COMUNITY LENDING, INCORPORATED, a) Chapter 11
3 California corporation,)
4) Honorable James Ware
Debtor.)
Bankruptcy Case No. 08-50030 (MM)
5)
MAI CHRISTINA PHAM, JOHN PHAM, MAI)
6 NGUYEN, HUNG PERRY NGUYEN, and) Adv. Proc. No. 08-05006
7 JOYCE FREEMAN,)
Plaintiffs,)
vs.)
COMUNITY LENDING, INCORPORATED, a)
9 California corporation, and Does 1 through 10,)
10 inclusive,)
Defendants.)
11)
12)
MEMORANDUM OF POINTS AND
AUTHORITIES IN SUPPORT OF
PLAINTIFFS' AND COUNTER-
DEFENDANTS' MOTION FOR
SUMMARY JUDGMENT
Date: September 22, 2008
Time: 9:00 a.m.
Courtroom: 8, 4th Floor

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Case No. C 08-00201 JW

MPA ISO MOTION FOR SUMMARY JUDGMENT

TABLE OF CONTENTS

	<u>Page</u>
INTRODUCTION & SUMMARY OF ARGUMENT	1
SUMMARY OF FACTS	2
A. Plaintiffs' Participation in the Plan.....	2
B. The Company's Misappropriation and Conversion of Plaintiffs' Plan Benefits	3
C. Procedural History	3
ARGUMENT	4
I. PLAINTIFFS ARE ENTITLED TO SUMMARY JUDGMENT ON THEIR FIRST AND THIRD CAUSES OF ACTION	4
A. The First and Third Causes of Action.....	4
B. The Undisputed Facts Establish that Plaintiffs Are Entitled to Payment of Their Benefits upon Termination of the Plan	4
C. The Company Was Solvent When the Plan Terminated	6
II. PLAINTIFFS' PLAN BENEFITS ARE NOT PROPERTY OF THE BANKRUPTCY ESTATE	7
CONCLUSION	8

1 **INTRODUCTION & SUMMARY OF ARGUMENT**

2 Plaintiffs and Counter-defendants Mai Christina Pham, John Pham, Mai Nguyen, Hung
 3 Perry Nguyen, Joyce Freeman, and Christopher Hake respectfully ask the Court to grant summary
 4 judgment in their favor on the First and Third Causes of Action. Each of those claims seeks to
 5 establish that Defendant ComUnity Lending Inc. (“Company”) is obligated to pay Plaintiffs their
 6 benefits pursuant to the Company’s Non-Qualified Deferred Compensation Plan (“Plan”).

7 Plaintiffs were employees of the Company and members of the Plan. Plaintiffs deferred
 8 over \$4.6 million of their earned salaries in reliance upon the Company’s promise that it would
 9 repay that money when they left the Company or when the Plan was terminated. Under the express
 10 terms of the Plan, upon termination of the Plan, Plaintiffs had an unqualified right to immediate
 11 payment of their Plan benefits. Section 10.2 of the Plan provides: “Upon termination of the Plan,
 12 the Participant’s full Compensation on a non-deferred basis will be thereupon restored.” Section
 13 8.13 of the Plan provides that Plaintiffs’ Plan benefits “are immediately payable in a lump sum
 14 upon a Plan Termination.”

15 On August 10, 2007, the Company’s Board unanimously voted to terminate the Plan,
 16 thereby immediately restoring Plaintiffs’ compensation on a non-deferred basis. Instead of paying
 17 Plaintiffs their benefits, however, the Company inexplicably concealed the Plan’s termination. On
 18 September 7, 2007, the Company finally revealed that the Plan had terminated. Plaintiffs
 19 accordingly instructed the Plan’s trustee to disburse their funds directly to their accounts. The
 20 Company then altered those instructions and instructed the trustee to pay the benefits directly to the
 21 Company instead. Months after the trustee had paid Plaintiffs’ Plan benefits to the Company, the
 22 Company claimed that it was “insolvent” and could not pay Plaintiffs, even though its financial
 23 statements stated the exact opposite.

24 On October 24, 2007, Plaintiffs filed an action in this Court to recover their Plan benefits.
 25 Almost one month later, the Company “restated” its financials to say that it was insolvent “as of
 26 September 30, 2007.” Plaintiffs believe that the Company will claim that its “restated” financials
 27 create a fact issue to impede the resolution of this action. However, sections 8.13 and 10.2 of the
 28 Plan restore Plaintiffs’ deferred salaries **without qualification**. They are not contingent upon the

1 Company's solvency. Moreover, it is undisputed that the Plan terminated on August 10, 2007. The
 2 Company's "restated" financial statement states that the Company was solvent at that time.
 3 Because the Company had no right to seize and convert Plaintiffs' Plan benefits, those benefits
 4 have been held in constructive trust since the Plan terminated and should be returned to Plaintiffs.

5 For all of these reasons, there is no disputed issue of material fact, and Plaintiffs are entitled
 6 to judgment as a matter of law.

7 **SUMMARY OF FACTS**

8 **A. Plaintiffs' Participation in the Plan**

9 Plaintiffs are former employees of the Company, which was engaged in the real estate
 10 mortgage and lending business. (Declarations of Mai Christina Pham ("M. Pham Decl.") ¶ 2; John
 11 Pham ("J. Pham Decl.", ¶ 2); Mia Nguyen ("M. Nguyen Decl.") ¶ 2; Hung Perry Nguyen ("H.
 12 Nguyen Decl.") ¶ 2; Christopher Hake ("Hake Decl.") ¶ 2; Joyce Freeman ("Freeman Decl.") ¶ 2.)
 13 During their employment, Plaintiffs deferred substantial portions of their salaries by contributing
 14 them to the Plan. The Company drafted the Plan Agreement (Pham Decl. ¶ 4, Ex. 1), and Investors
 15 Bank & Trust Company ("IBT"), as trustee, administered by pursuant to a separate Trust
 16 Agreement. (*Id.* ¶ 5, Ex. 2.)

17 All of the money in the Plan came from employees' voluntary contributions of their
 18 salaries, and the accrued interest thereon. When the Company terminated the Plan, Plaintiffs' Plan
 19 accounts had the following aggregate balances:

<u>Plaintiff</u>	<u>Account balance</u>
John Pham	\$1,552,926.30
Mai Christina Pham	1,805,630.82
Hung Perry Nguyen	214,441.68
Mai Nguyen	262,120.47
Joyce Freeman	407,893.68
Chris Hake	<u>413,187.75</u>
TOTAL	\$4,656, 200.75

27 (M. Pham Decl. ¶ 3; J. Pham Decl. ¶ 4; M. Nguyen Decl. ¶ 4; H. Nguyen Decl. ¶ 4; Freeman Decl.
 28 ¶ 4; Hake Decl. ¶ 4.)

1 On August 10, 2007, the Company's Board of Directors terminated the Plan. (Declaration
 2 of Matthew Borden ("Borden Decl.") ¶ 3, Ex. 1; Answer to Verified Complaint ("Answer") ¶ 23.)
 3 According to the Company's own financial records, as of that date, the Company was solvent.
 4 (Borden Decl., Ex. 2.)

5 On September 7, 2007, the Company issued a Termination Announcement dated September
 6 4, 2007 ("Termination Announcement"). (Pham Decl., Ex. 3.) The Termination Announcement
 7 informed Plan members for the first time that the Company had terminated the Plan. (*Id.* ¶ 6.)

8 **B. The Company's Misappropriation and Conversion of Plaintiffs' Plan Benefits**

9 After receiving notice of the Plan's termination, Plaintiffs filled out distribution request
 10 forms to IBT's Plan Administrator, Transamerica. (Pham Decl., Ex. 4.) The Company modified
 11 those instructions and without Plaintiffs' knowledge or consent and instructed the trustee to divert
 12 the funds to the Company, rather than transmitting them to Plaintiffs, as Plaintiffs had requested.
 13 (*Id.* ¶ 8, Ex. 4.)

14 By no later than September 17, 2007, IBT had distributed Plaintiffs' Plan benefits directly
 15 to the Company instead of to all of the Plaintiffs except Christopher Hake. (Pham Decl. ¶ 9.)¹
 16 After receiving Plaintiffs' Plan benefits from IBT, the Company failed to distribute the Plan
 17 benefits to Plaintiffs and, instead, improperly diverted all the Plan's assets to the Company's own
 18 accounts. (*Id.* ¶ 10.) Thereafter, the Company refused to pay Plaintiffs their Plan benefits. (*Id.*)

19 **C. Procedural History**

20 On October 24, 2007, Plaintiffs filed suit in this Court against the Company. In response
 21 to Plaintiffs' application for a temporary protective order ("TPO") and writ of attachment, the
 22 Company filed a declaration stating that the Company purportedly had "restated" its finances to
 23 claim that it was insolvent as of September 30, 2007. (Borden Decl., Ex. 1.) On November 20,
 24 2007, this Court entered a TPO, prohibiting Defendant from dissipating Plaintiffs' Plan assets. (*Id.*,
 25 Ex. 3.) On December 6, 2007, after a further hearing, this Court entered an Order Granting

26 ¹ For some reason, Mr. Hake's Plan benefits were distributed to the Company after September 17,
 27 2007. The Company refused to return those benefits as well. (Hake Decl. ¶ 5.)

1 Plaintiffs' Application for a Writ of Attachment and issued a Writ of Attachment. (*Id.*, Ex. 4.)

2 Since that time, Plaintiffs' Plan benefits have remained in two separate segregated accounts.

3 On January 4, 2008, the Company commenced a bankruptcy case. On January 11, 2008,
 4 Plaintiffs filed an adversary proceeding in Bankruptcy Court alleging causes of action for breach of
 5 contract and declaratory relief. On April 7, 2008, this Court withdrew its reference of the matter to
 6 the Bankruptcy Court as to this adversary proceeding. (Borden Decl. ¶ 8.)

ARGUMENT

8 Summary judgment is proper if the "pleadings, depositions, answers to interrogatories, and
 9 admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any
 10 material fact and that the moving party is entitled to judgment as a matter of law." Fed. R. Civ. P.
 11 56(c); *Celotex Corp. v. Catrett*, 477 U.S. 317 (1986).

I. PLAINTIFFS ARE ENTITLED TO SUMMARY JUDGMENT ON THEIR FIRST AND THIRD CAUSES OF ACTION

A. The First and Third Causes of Action

14 In their First Cause of Action, Plaintiffs allege that the Company breached the Plan by
 15 seizing Plaintiffs' Plan benefits, instead of paying them to Plaintiffs when the Company terminated
 16 the Plan. In their Third Cause of Action, Plaintiffs seek a declaration that pursuant to the terms of
 17 the Plan, Plaintiffs are entitled to their Plan benefits.

B. The Undisputed Facts Establish that Plaintiffs Are Entitled to Payment of Their Benefits upon Termination of the Plan

20 Interpretation of a contract is a matter of law for the Court to determine. *See, e.g., United*
 21 *States Cellular, Inv. Co. of L.A. Inc. v. GTE Mobilnet, Inc.*, 281 F.3d 929, 934 (9th Cir. 2002)
 22 (interpretation of a contract is a matter of law); *Davis v. Yageo Corp.*, 481 F.3d 661, 673 (9th Cir.
 23 2007) ("The interpretation of the language in a contract is a question of law reviewed de novo.").

24 Under the plain language of the Plan, Plaintiffs had an unqualified right to receive their Plan
 25 benefits upon termination of the Plan. Section 10.2 of the Plan provided that "Upon termination of
 26 the Plan, the Participant's full Compensation on a non-deferred basis will be thereupon restored."
 27 Section 8.13 of the Plan provided that benefits are "are immediately payable in a lump sum upon a
 28 Plan Termination." (Pham Decl., Ex. 1.)

1 In an attempt to avoid paying Plaintiffs their benefits, the Company argues that it was not
 2 required to pay Plaintiffs their Plan benefits because it was allegedly insolvent at whatever point in
 3 time it decided to repay them. But whether the Company was insolvent is irrelevant to Plaintiffs'
 4 rights under Sections 10.2 and 8.13. Those provisions expressly govern what must occur when the
 5 Plan terminates, and both of them give Plaintiffs an unqualified right to the portions of their salary
 6 that they had deferred at the time the Plan terminated. Section 10.6, upon which Defendant relies,
 7 generally provides that Plan monies are subject to the claims of general creditors, but that provision
 8 only applies where the Plan is in effect, not when it has been terminated.

9 Plaintiffs' reading of the plain language of the Plan is consistent with the overall purpose
 10 and structure of the Plan and all other deferred compensation plans. The purpose of deferred
 11 compensation plans is to allow participants to defer paying tax based on Internal Revenue Code
 12 § 83. That provision states that money paid in exchange for services is taxable once it is no longer
 13 subject to a "substantial risk of forfeiture." 26 U.S.C. § 83(a)(1); 26 C.F.R. § 1.83-3; *see also*
 14 *Minor v. United States*, 772 F.2d 1472, 1475 (9th Cir. 1985). While the Plan was in effect, there
 15 was a substantial risk of forfeiture because the funds were subject to claims by the general
 16 creditors. However, once the Plan was terminated, there was no need for any further risk of
 17 forfeiture. At that point in time, the salary payments were immediately "restored" to the
 18 participants on a "**non-deferred basis**" and were no longer capable of divestment.

19 This conclusion is buttressed by a comparison of the Plans' two separate vesting provisions,
 20 which treat vesting differently when the Plan is in effect, as opposed to after it has been terminated.
 21 Section 7.1 provides that while the Plan is in effect, a participant's rights are subject to those of the
 22 employer's creditors. It states: "The value of a Participant's Account shall be fully vested at all
 23 times subject, however, to the reach of the Employer's creditors in the event of insolvency."
 24 However, the Plan further explains that "Upon the termination of the Plan, all participants will be
 25 100% vested," without reference to any qualifications whatsoever. (Pham Decl., Ex. 1 § 10.2.)
 26 Read together, sections 7.1 and 10.2 reinforce the plain language and purpose of the Plan that **prior**
 27 **to** the Plan's termination, Plan participants' rights are subject to claims of the Company's creditors,
 28 but **after** termination of the Plan, Plan members have a categorical right to their Plan benefits.

1 Finally, even if there were some ambiguity as to the meaning of Sections 10.2 and 8.13 –
 2 which there is not – any ambiguity must be construed against the Company as the drafters of the
 3 Plan. *See Blankenship v. Liberty Life Assurance Co.*, 486 F.3d 620, 625 (9th Cir. 2007) (applying
 4 doctrine of *contra proferentem* in construing ERISA plan). Here, it is undisputed that the Plan
 5 terminated on August 10, 2007. Plaintiffs became the owners of their Plan benefits on that date
 6 and were entitled to payment of those benefits immediately on a non-deferred basis.

7 **C. The Company Was Solvent When the Plan Terminated**

8 Plaintiffs also are entitled to summary judgment for the separate and independent reason
 9 that the Company was solvent at the time it terminated the Plan, at which point Plaintiffs' benefits
 10 were immediately due. The Company's financial statement shows that it was solvent as of August
 11 31, 2007. (Borden Decl., Ex. 2.) On November 17, 2007, almost one month *after* Plaintiffs filed
 12 suit against the Company and more than 3 months after the Plan was terminated, the Company's
 13 "Restructuring Officer" ordered a former officer to "adjust" the Company's financial statement
 14 based on "the Company's assets and liabilities as of September 30, 2007 based on a present day fair
 15 market valuation in light of the current factual circumstances." (Borden Decl., Ex. 1 ¶ 5.) The
 16 Company claims that its "adjusted" financial statement now shows that it was insolvent as of
 17 September 30, 2007. (*Id.* ¶ 5, Ex. A.)

18 These facts fail to establish a triable issue. The Plan indisputably terminated on August 10,
 19 2007, at which time the Company was solvent. Further, the Company undisputedly was solvent on
 20 September 4, 2007, when it claimed the termination "became effective." By September 17, 2007,
 21 IBT had paid all of Plaintiffs' (except Christopher Hake's) Plan benefits to the Company. The
 22 Company was undisputedly solvent on that date, too.²

23 The Plan specifically states: "Benefits under this Plan are immediately payable in a lump
 24 sum upon a Plan Termination." (Pham Decl., Ex. 1 § 8.13.) That provision required payment to

25 ² The Company never provided notice of insolvency as it was required to do under section 3(b)(1)
 26 of the Trust, which reads: "The Board of Directors/Trustees and Chief Executive Officer on behalf
 27 of the Employer shall have the duty to inform the Trustee in writing of the Employer's
 Insolvency."

28

1 Plaintiffs, and did not permit the Company to attempt to deprive Plaintiffs of their rights through
 2 delay. *See Stillman v. LaMarque*, 319 F.3d 1199, 1202 (9th Cir. 2003) (quoting The American
 3 Heritage College Dictionary 679 (3d Ed. 1997)) (“‘Immediately’ means ‘without delay.’”). This is
 4 especially true where, as here, the immediate payment is from an employee benefit plan to
 5 employees who have retired or left the Company.

6 For this separate reason, Plaintiffs are also entitled to summary judgment on their First and
 7 Third Causes of Action.

8 **II. PLAINTIFFS’ PLAN BENEFITS ARE NOT PROPERTY OF THE BANKRUPTCY
 9 ESTATE**

10 Under 11 U.S.C. § 541(d), “property of the estate” excludes “[p]roperty in which the debtor
 11 holds, as of the commencement of the case, only legal title and not an equitable interest” *See*
In re Unicom Computer Corp., 13 F.3d 321, 324 (9th Cir. 1993) (“something held in trust by a
 12 debtor for another is neither property of the bankruptcy estate under section 541(d), nor property of
 13 the debtor for purposes of section 547(b)”). Because a debtor has no equitable interest in it,
 14 property held in constructive trust is not property of the estate. *Id.* (“In the instant case, we are
 15 dealing with a particular type of trust, *viz*, a constructive trust”); *In re Coupon Clearing Serv.*, 113
 16 F.3d 1091, 1099 (9th Cir. 1997) (citations omitted) (“Property that is held in trust by a debtor for
 17 another, however, is not property of the estate. This rule of law applies with equal force to
 18 constructive trusts”); *In re Advent Mgm. Corp.*, 104 F.3d 293, 295 (9th Cir. 1997) (“In the
 19 case of funds held by a debtor in constructive trust for another person, the equitable interest in the
 20 trust funds belongs to the trust beneficiary not the debtor.”); *Elliott v. Bumb*, 356 F.2d 749, 753 (9th
 21 Cir. 1966).

22 Plaintiffs’ Plan benefits are not property of the estate because the Company has held them
 23 in constructive trust for Plaintiffs’ benefit since the termination of the Plan. The broad remedial
 24 provisions of ERISA enable the Court to impose a constructive trust over wrongfully withheld
 25 benefits. *E.g.*, *Waller v. Blue Cross*, 32 F.3d 1337, 1339 (9th Cir. 1994) (quoting (*Amalgamated*
Clothing & Textile Workers v. Murdock, 861 F.2d 1406, 1419 (9th Cir. 1988)) (alteration in
 26 original) (“‘ill-gotten profits [are] held in a constructive trust for plan participants and beneficiaries
 27 28

1 [and] may be construed as equitably vested benefits under an ERISA plan””). Such a remedy is
2 necessary here given the Company’s wrongful seizure and conversion of Plaintiffs’ funds.

3 **CONCLUSION**

4 For the foregoing reasons, there is no issue of material fact, and Plaintiffs are entitled to
5 judgment as a matter of law on their First and Third Causes of Action.

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7 Dated: June 16, 2008

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9 By: _____ /s/
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